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RUEHKSO/AMCONSUL SAPPORO 2226
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RUEHNH/AMCONSUL NAHA 4017
RUEHGH/AMCONSUL SHANGHAI 0516
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C O N F I D E N T I A L TOKYO 003542

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TAGS: EINV EFIN PGOV JA
SUBJECT: JAPAN'S LOWER FDI INFLOWS REFLECT GLOBAL FINANCIAL
TURMOIL

REF: A. TOKYO 3417
¶B. TOKYO 1421

Classified By: Charge d'Affaires James P. Zumwalt. Reason 1.4(b)(d)

¶1. (SBU) Summary: Japan's foreign direct investment (FDI) inflows in the first ten months of 2008 declined year-on-year for the first time since 2003, reflecting the impact of global financial market turmoil and following record inflows in 2007. Preliminary Ministry of Finance (MOF) figures show Japan's FDI inflows between January 1 and October 31, 2008 were 14 percent below the same period in 2007. While December 30 press articles report a more dramatic 36 percent decline, these reports significantly exaggerated the drop. The comparision period the journalists used included two exceptionally strong months in 2007, while excluding January 2008, a month in which Japan received a near-record inflow of 1.4 trillion yen, reflecting, in part, the closing of the USD 18 billion Nikko-Citigroup merger. End Summary.

¶2. (SBU) Throughout 2008, Japan saw a gradual but persistent slowdown in FDI inflows. Monthly FDI inflows in CY2008 averaged 600 billion yen, compared with a record-high average 666 billion yen per month in CY2007. The slowdown accelerated in the second half of the year. Between July and October 2008, monthly inflows averaged only 350 billion yen. Statistics for Japan-related merger and acquisition (M&A) activity in the same period show a similar trend. Between January and November 2008, M&A deals involving Japanese firms fell 10.2 percent by volume, according to the private sector consultancy Recof, although the total value of transactions was up a marginal 6.6 percent. The largest decline came in the number of "out-in" transactions -- in which a foreign buyer acquires a Japanese firm; these declined 36 percent.

¶3. (C) With credit increasingly difficult, 2008 is likely to be the worst year for Japanese M&A since 2003. The financial and the real estate sectors, two historically strong areas for FDI, lead the current downturn. The American head of a Tokyo-based investment fund with significant investments in Japan's real estate sector told us recently Japanese banks have effectively cut off Japan-based real estate investment trusts from all short-term funding. Their goal is to avoid a repeat of 1990's when falling real estate prices brought Japan's banking system to its knees.

¶4. (C) Japanese officials responsible for FDI promotion have anticipated a downturn in FDI flows for some months. Hiroki Hara, Cabinet Office Director of Investment Promotion, admitted to Emboff in early December the goal of increasing Japan's FDI stock to the equivalent to five percent of GDP by the end of FY2010 (March 2011) now appears all but impossible, even though it remains official GOJ policy. (Note: According to MOF figures, Japan's FDI stock at the end of September 2008 was 17.01 trillion yen or about 3.3 percent of current real GDP. End note.) Hara complained that since Minister of Economic and Fiscal Policy Hiroko Ota left office in the September 2008 government realignment, no one in the cabinet has a strong interest in investment issues. Nonetheless, his office continues work on a new national investment strategy -- the first since June 2006 -- as called for in the government's June 2008 Economic and Fiscal Policy Report. Drawing from recommendations of the Cabinet's ad-hoc Investment Experts Committee (Ref B), the new strategy will focus on ways to stimulate more balanced growth by attracting FDI to Japan's other regions besides Tokyo, and seek ways to draw FDI into priority sectors, including production of medical devices. The strategy report should be ready for Cabinet approval in January 2009, Hara said.
ZUMWALT